> facilities and capabilities (*e.g.*, central office switching) will likely need to be obtained from the incumbent local exchange carrier as network elements pursuant to Section 251. Nonetheless, the conference agreement includes the "predominantly over their own facilities" requirement to ensure a competitor's offering service exclusively through the resale of a BOC's telephone exchange service does not qualify and that an unaffiliated competing provider is present in the market.[73]

If Congress believed that resale-based competition would constitute sufficient local competition to the BOCs to preclude exploitation of their market power, there would have been no need to condition removal of the interLATA restriction on the presence of a facilities-based competitor. A "presence of any competitor" test (including pure resale competitors) could have been included instead.

Similarly, the Commission itself historically has viewed resale primarily as a mechanism for restraining the pricing behavior of monopoly carriers, rather than as a means for promoting competition from those carriers. Despite requiring the resale of interstate common carrier services for two decades, the Commission never has deemed resale to constitute significant competition to traditional carriers. In the Commission's seminal Resale and Shared Use decision,[74] the Commission concluded that prohibitions

[73]H.R. Rep. No. 458, 104th Cong., 2nd Sess. at 148 (1995).

[74]Resale and Shared Use of Common Carrier Services, 60 FCC2d 261 (1976), *recon.* 62 FCC2d 588 (1977), *aff'd. sub nom.* American Telephone and Telegraph Company v. FCC, 572 F.2d 17 (2d Cir. 1978), *cert. den.* 439 U.S. 875 (1978).

on the resale of common carrier services were unjust and unreasonable. It embraced resale as a means to discipline regulated monopoly carriers to base their prices on cost, rather than as a means to stimulate competition in the provision of services offered by such carriers.[75]

From the foregoing, it should be apparent that the 1996 Act reflects Congress's perception that meaningful competition to the local services of ILECs, especially the BOCs, will eventuate through the development of additional facilities-based networks, and through the introduction of services provided over those competing networks, not through the resale and repackaging of services provided over ILEC networks, either by resale of retail services obtained at wholesale rates or by provision of services comprised entirely of unbundled network elements obtained from ILECs. In promulgating regulations to guide the states in determining wholesale prices for ILEC retail services, the Commission should remain mindful of the central role of facilities-

[75]The Commission stated:

> Removal of these tariff restrictions on resale and sharing would create further pressures on carriers to provide their services at rates which are wholly related to costs. When similar services are available from a single carrier, but one service is available in unit quantities while the other service is available on a bulk discount basis, resale and sharing of the bulk quantity service would compel the carrier to price the bulk offering at rates wholly related to cost savings in providing the bulk quantity. Id. at ¶75.

based networks in the advent of local competition, and it should be careful not to sanction requirements which result in wholesale rates for ILEC services being so low as to discourage investment in competing networks and to stimulate artificially resale market entry even where such market entry is not efficient.

To illustrate the importance of facilities-based competing networks to the development of local competition, Attachment 4 to these comments is a table which provides a comparison of operating margins for residential and business exchange services with 40%, 25%, and 10% discount levels for wholesale service. The analysis takes into account the cost of facilities-based interconnection compared with the cost of resale. Facilities-based providers incur costs associated with interconnection, number portability, property taxes, outside plant investment, and other start-up costs that resellers do not incur. In addition, while it takes considerable time for facilities-based providers to achieve scale economies through facility utilization, resellers are virtually guaranteed full utilization from the outset. Moreover, since resellers have no local exchange network investment, any positive cash flow represents an infinite return on investment with no risk to the recovery of shareholder investment. Resellers could be nothing more than a "desk-top" operation by simply branding a facilities-based carrier's basic exchange services. Therefore, resellers should be expected to operate on very low margins much like other non-capital intensive businesses, such as a grocery store. This is in stark contrast to capital intensive industries, like telecommunications network services, which need higher margins because of their highly capital intensive nature and low asset turnover.

The comparison on Attachment 4 indicates that operating margins for residential resale greatly exceed -- by eight times -- that of facilities-based service even at a wholesale rate at 90% of the retail rate. This comparison, after accounting for the fixed capital costs and one-time start-up costs incurred by a facilities-based provider, is even more dramatic.

For business exchange service, operating margins break even at approximately a 25% discount, but fall well below those of resale when capital costs are considered. It must be remembered that even equivalent operating margins have a very different financial impact on those firms with substantial infrastructure investment as compared with those firms that do not.

While the 1996 Act is clear and specific that wholesale rates are to be based on retail rates less avoided costs, the above analysis demonstrates the importance of not overstating the level of avoided costs and of ensuring that all relevant wholesale costs are included in wholesale rates. Only in this way can the Commission assure that the resulting wholesale rates will not serve as a disincentive to investment in facilities-based networks. In addition, these relationships should also be considered in the Commission's decisions on reciprocal compensation and number portability. Specifically, as discussed later in these comments, the Commission should require bill-and-keep as the preferred method of reciprocal compensation to avoid the necessity of facilities-based providers building costly measurement and billing systems for mutual call termination. Finally, the Commission should note that interim number portability will cost facilities-based providers over $5.00 per month for each residential line and over $10 per month for each business line with ported numbers.[76] Therefore, the Commission must immediately declare that full number portability via the Local Routing Number solution is "technically feasible" and require LECs to begin deployment of full number portability by the end of 1997.[77]

Based upon the foregoing concerns, several resale-related issues raised in the Notice warrant specific comment by TW Comm. At ¶176 of the Notice, the Commission inquires whether discounted

[76]These costs represent the rates charged by ILECs for Remote Call Forwarding and the access revenue lost to the dialtone provider because it is billed and retained by the ILEC. Also, the Commission should consider requiring ILECs to remit the terminating access revenues to the terminating carrier since the Commission's access charge rules contemplate that the carrier terminating the end users' traffic receive the access revenues. Where the traffic is being terminated by a competing LEC, that LEC, not the ILEC, is performing the terminating access function and is therefore entitled to the terminating access revenue.

[77]See Further Comments of Time Warner Communications Holdings, Inc., CC Docket No. 95-116, March 29, 1996.

and promotional offerings of ILECs should be subject to the resale at wholesale rate requirement of Section 251(c)(4). Nothing in that section suggests that every rate for every ILEC service should be reduced to a wholesale rate for purposes of resale. By its terms, the resale at wholesale rate obligation codified at Section 251(c)(4) is applicable to "any telecommunications <u>service</u> that the carrier provides at retail to subscribers who are not telecommunications carriers" (emphasis added). The fact that the requirement is applicable to every service, rather than every rate charged for each service, is significant.

It is not unusual for carriers, including ILECs, to offer service to retail customers at a multiplicity of rates. Such rates vary depending on factors like term and quantity commitments, calling patterns, whether customers are "business" or "residential" customers, etc. Not every rate for every service charged to every customer recovers the same costs. This is especially true for certain discounted or promotional rates which often are only available for limited periods of time or to limited classes of customers. If every discounted or promotional rate were to be made available at wholesale rates for resale to telecommunications carriers, the result would be a proliferation of resold service offerings at rates well below any reasonable measure of cost of providing service. Mandatory availability of below cost services to end users was not Congress's intent in formulating the resale requirements of Section 251(c)(4). Moreover, such below cost availability of service to consumers would impede development of meaningful facilities-based competition.

TW Comm agrees with the Commission that Section 251(c)(4)(B) should be read to enable a state to preclude services available to certain categories of subscribers from being offered on a resale basis to different categories of subscribers.[78] This requirement becomes especially important with respect to ILEC services which are the recipients of subsidization either by other ILEC services, or by other carriers' services. For example, in many states, residential local exchange service is priced at rates lower than business local exchange service. To require that residential service be offered to resellers at wholesale rates for resale to business customers would undermine the basis for the pricing distinction between residential and business services. Similarly, under the current universal service rules,[79] certain ILECs serving high cost areas receive funds from interstate toll services to be used for the purpose of maintaining local service rates at levels reasonably close to the national average rates. Those local

[78]Section 251(c)(4)(B) provides, in relevant part, that "a state commission may, consistent with regulations prescribed by the Commission under this section, prohibit a reseller that obtains at wholesale rates a telecommunications service that is available at retail only to a category of subscribers from offering such service to a different category of subscribers."

[79]47 C.F.R. §36.631 *et seq.*

service rates which are supported by contributions from the Commission's Universal Service Fund program should not be mandatorily available at wholesale rates for resale to end users who would not otherwise be entitled to subsidized rates.

1. The Avoided Cost Standard In Section 252(d)(3) Must Be Limited To Those Costs Which Are Truly Avoided By A LEC In Providing Wholesale Service For Resale

As noted above, Section 252(d)(3) requires that ILEC wholesale rates for purposes of resale are to be set on the basis of ILEC retail rates excluding the portion of those retail rates which are attributable to marketing, billing, collection and other costs which are avoided by the ILEC. In the Notice, the Commission states its belief that it is authorized to promulgate rules for the states to follow in applying the avoided cost standard of Section 252(d)(3).[80] In TW Comm's view, not only is the Commission authorized by the 1996 Act to establish rules for states to follow in implementing the avoided cost standard, but that the 1996 Act and the public interest goals underlying the 1996 Act compel Commission promulgation of nationally uniform rules for the states to follow in determining avoided costs.

The need for nationally uniform wholesale pricing rules based on a consistent application of the avoided cost standard is shown by the wide disparity in the manner in which states have

[80]Notice at ¶178.

established wholesale rates for ILEC services. To date, only a few state commissions have set wholesale prices for ILEC services for purposes of resale, and most of those have been established on an interim basis. Nonetheless, there have been wide variations in the wholesale prices mandated by state commissions. For example, California recently required Pacific Bell to offer wholesale rates for business and residential services at 17 percent and 10 percent below retail rates respectively, and required GTE -- the second largest ILEC in California -- to offer business and residential service for resale at wholesale rates at 12 percent and 7 percent below retail rates.[81] Tennessee has mandated on an interim basis a 25 percent discount below the retail rate for wholesale service to be resold. Illinois and Michigan have established interim discount ranges of 8 to 10 percent and 6 to 10 percent respectively. In New York, Rochester Telephone has established a 5 percent discount. In short, based upon the few states which have considered the issue, "appropriate" wholesale discounted rates have ranged from 5 percent to 25 percent -- a considerable disparity. This disparity demonstrates why a nationally uniform approach to establishing wholesale rates based upon a consistently-applied avoided cost standard must be in place to ensure that proper

[81]Order Instituting Rulemaking on the Commission's Own Motion Into Competition for Local Exchange Service, R.95-040043, Order Instituting Investigation on the Commission's Own Motion into Competition for Local Exchange Service, I.95-04-044. Decision (Cal. Pub. Util. Comm'n. March 13, 1996).

pricing signals are sent to the local resale market in all states.

The starting point for establishment of avoided cost rules is the statute itself:

> . . . a state commission shall determine wholesale rates on the basis of retail rates charged to subscribers for the telecommunications service requested, excluding the portion thereof attributable to any marketing, billing, collection, <u>and other costs that will be avoided</u> by the local exchange carrier.[82]

By its terms, "avoided costs" for the purpose of establishing wholesale rates are to be limited to those costs which are, in fact, avoided by an ILEC when it sells service to telecommunications carriers for resale rather than directly to consumers as a retail service. By definition, avoided costs should include nothing but those costs that are actually avoided by the ILEC when it provides wholesale service to telecommunications carriers. They must not include any "mark-up" or any assignment of general overhead costs, or any other cost component beyond costs actually avoided by the ILEC. Indeed, any cost component beyond costs which an ILEC actually avoids (*i.e.*, does not incur) when it sells a service at wholesale for eventual resale, rather than selling the service at retail directly to consumers, is not an "avoided cost" within the meaning of 252(d)(3) since those general overhead costs would be incurred by the ILEC even if it did not provide wholesale service.

[82] 47 U.S.C. §252(d)(3) (emphasis added).

The avoided cost standard of Section 252(d)(3) is properly a net avoided cost standard. That is, the wholesale rate should be based on the retail rate less only those costs which are actually avoided by the ILEC. However, under the avoided cost standard, the wholesale rate must also include costs which are incurred by the ILEC in providing the wholesale service, but which would not be incurred by the ILEC to provide the same service at retail.[83] In telecommunications, as in other businesses, vendors often incur additional costs in selling services and products to large customer market segments, such as a wholesale market. For example, in the interexchange services market where a resale market segment has existed for many years, those facilities-based carriers which sell to that market segment incur substantial investments and expenses to develop the infrastructure to service the resale market. AT&T, by far, the leading interexchange reseller, has done so as have other IXCs. Information contained in an evidentiary record of a recent state proceeding illustrates this point. In responding to a data request in a proceeding before the Tennessee Public Service Commission, AT&T stated as follows:

> AT&T has established a dedicated organization (Specialized Markets Directorate) as the sales channel and account support organization that serves customers

[83]Alternatively, a cost standard could include rules to price new or additional services and functions required of the ILEC to serve resellers. These services and functions may include, but not be limited to, mechanized ordering systems, new billing data feeds, installation systems interfaces.

> engaged in the resale of AT&T service. Resellers can place orders for AT&T service through the SMD by U.S. mail, e-mail, or by diskette. Resellers are aided by a manual prepared by SMD which contains sample ordering forms, ordering reports, procedures, and contact numbers. Upon receipt of a completed order, SMD then forwards the order to the appropriate provisioning organization, depending on the particular service ordered. The reseller's order is provisioned along with that of other commercial customers for the same service.[84]

Similarly, the extensive "carrier services" infrastructures created by ILECs to market and provision services, including access services, to their carrier customers is illustrative of the significant additional costs incurred in order to serve wholesale markets or resale markets. While an ILEC may incur marketing, billing, collection and other costs in serving the wholesale segment of a market that differ from those which it incurs in serving the retail segment, it does incur costs. In some instances, those costs may be as great as or even greater than those expended in servicing retail customers. Certainly, ILECs, like AT&T in the interexchange market, will incur marketing and advertising expenses, and will incur billing, collection and other costs to serve wholesale customers. In order to prevent subsidized, below cost prices for wholesale services available for resale, it is imperative that the "wholesale" prices mandated by

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[84]AT&T Response to First Data Requests, Item 20, of BellSouth in Tennessee Public Service Commission Docket No. 96-00067. In response to Item 13 of the same data request, AT&T admitted removing all <u>retail</u> marketing and customer operations expenses without replacing those expenses with any <u>wholesale</u> expenses.

Section 251(c)(4) established in accordance with the avoided cost standard of Section 252(d)(3) reflect all costs incurred (and therefore not avoided) by the ILEC in providing service.

Other examples where AT&T has deleted retail costs without accounting for corresponding wholesale costs include uncollectible costs and billing costs. It is completely unreasonable to expect that uncollectible costs will be totally eliminated as a result of providing service to resellers at wholesale instead of end users at retail. While resellers must absorb the cost of non-payment on the part of their end users, some resellers will experience financial difficulties, go out of business, or fail to pay their bills for various other reasons. Indeed, the California Public Utilities Commissions recently cited a case of a reseller that went into bankruptcy owing Pacific Bell and GTE of California millions of dollars.[85] In addition, while retail billing costs associated with the printing and mailing of invoices to end users are avoided in a resale situation, wholesale costs for the processing, printing, and mailing of invoices to resellers are incurred by ILECs and must be included. Such conclusions were reached by the California PUC, which identified four major areas where AT&T's methodology was flawed, including the allocation of one hundred percent of marketing, customer services, and uncollectible costs to the retail

[85] Order Instituting Rulemaking on the Commission's Own Motion Into Competition for Local Exchange Service, R.95-04-043, Decision 96-03-020, March 13, 1996 at 29.

operation.[86]

At ¶180 of the Notice, the Commission expresses concern that a system of determining wholesale rates based on ILECs' actual avoided costs would create administrative difficulties because the information regarding those costs is under the control of the ILECs. Alternatively, the Commission proposes to allow states to determine avoided costs based upon a uniform set of presumptions.[87] In TW Comm's view, determining wholesale rates under the avoided cost standard on a system of presumptions is neither necessary nor consistent with the statute. While it is correct that ILEC cost information, including avoided cost information, is within the ILEC's possession, virtually all state commissions have the authority to compel the ILECs to demonstrate their avoided costs. Nothing in the statutory language or the 1996 Act's legislative history indicates that Congress intended to base the avoided cost standard on anything other than actually avoided costs. There does not appear to be any statutory basis for attempting to approximate avoided costs based on presumptions, proxy factors, allocators (with or without allocations of common costs), or any other mechanism, instead of identifying and quantifying actually avoided costs.

A system which allocates avoided costs across services, as

[86] *Id.*

[87] Notice at ¶181.

suggested at ¶182 of the Notice, would result in certain costs being excluded from the wholesale prices of specific services which are not in fact avoided by the ILEC in providing those services. Among the different services provided by ILECs at retail rates to consumers, there are differences in costs incurred and there are corresponding differences in costs avoided when those services are provided at the wholesale level rather than the retail level. Certain ILEC services are considered by consumers to be necessary components of telephone exchange service while other services may be viewed by consumers as less necessary, and therefore more discretionary. Those services deemed to be more discretionary should be subject to relatively higher marketing costs than those services deemed to be essential components of local service.

For example, local dialtone service is considered by consumers to be a necessary aspect of local service, and it is therefore not necessary for an ILEC to expend significant resources marketing that service. Conversely, services like caller identification, call waiting, and three-way calling probably necessitate higher sales and marketing expenditures by ILECs to persuade consumers to acquire those services. Thus, it would send misleading signals to the resale community for ILECs to allocate comparable avoided costs to basic dialtone service as are allocated to a discretionary service like call waiting. The wholesale price for local dialtone service should be determined based on retail price less the costs avoided in providing dialtone service to resellers. The wholesale price for call waiting should be determined based on the retail price less the costs avoided by the ILEC in providing call waiting service to resellers.

2. Relationship Between Wholesale Rates And Rates For Unbundled Network Elements

The Commission seeks comment on the appropriate relationship between wholesale rates established pursuant to the avoided cost standard codified at Section 252(d)(3) (discussed above) and the rates for unbundled network elements. Some states have adopted an "imputation rule" which precludes the sum of the applicable network element rates from exceeding the retail service rate for service comprised of the same unbundled network elements.[88]

Where network element rates are established based upon TSLRIC (as they should be), it is unlikely that they would exceed retail service rates. Where, however, retail rates are priced below TSLRIC costs, pursuant to state regulator-mandated subsidization policies (*e.g.*, as is often the case with respect to residential local service rates), unbundled network element rates based on TSLRIC may exceed the retail rate for a corresponding subsidized service. In the Notice, the Commission suggests that an imputation rule is not necessary in such circumstances since a competing local

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[88]Notice at ¶184.

service provider could charge above-cost prices for such services as intrastate toll and exchange access to support below cost subsidized services in the same manner as the ILEC.[89]

As a threshold matter, TW Comm notes that once those services which support subsidies become competitive, it is unlikely that the competing providers will ignore competitive forces and uniformly retain non-competitive margins in order to support residential service priced below TSLRIC. The proper solution is to rebalance basic service rates and to remove those implicit subsidies. To the extent that subsidization or assistance remains necessary to ensure universally affordable local service -- a policy mandated by the 1996 Act and one which TW Comm wholeheartedly endorses -- such subsidization should be explicitly provided and should be established in accordance with the rules being considered by a Federal-State Joint Board in CC Docket No. 96-45 to implement the universal service requirements of Section 254 of the Act.[90] TW Comm recognizes that there will be a period of approximately nine months between completion of the instant proceeding and completion of the Joint Board proceeding on universal service. Accordingly, TW Comm agrees with the Commission that during this transition an imputation rule is not necessary. The application of the rule,

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[89] Notice at ¶186.

[90] Federal State Joint Board on Universal Service (*Notice of Proposed Rulemaking and Order Establishing Joint Board*), FCC 96-93, released March 8, 1996.

once a new universal service mechanism is established, should include in the equation any universal service funding mandated by that mechanism.

G. Reciprocal Compensation For Transport And Termination Of Traffic

1. Reciprocal Compensation For "Transport and Termination" As Set Forth In Section 251(b)(5) Includes Traffic Between LECs In The Same And Adjacent Service Areas

While Section 251 of the 1996 Act sets forth a general framework governing interconnection between and among telecommunications carriers, Section 251(b)(5) specifically imposes a duty on all LECs to "establish reciprocal compensation arrangements for the transport and termination of telecommunications." As a threshold matter, the Notice seeks comment on whether "transport and termination of telecommunications" only encompasses traffic that originates on the network of one LEC and terminates on the network of a competing LEC in the same local service area (including traffic passing between LECs and CMRS providers) or also encompasses traffic passing between neighboring LECs that do not compete with one another.[91]

TW Comm submits that the reciprocal compensation requirement for the transport and termination of telecommunications traffic applies both to competing and non-competing LECs in the same local

[91]Notice at ¶230.

service area, and adjacent service areas (*i.e.*, Extended Area Service or "EAS" traffic).[92] The statute makes no distinction between competing and non-competing LECs, and neighboring LECs that currently do not compete are likely candidates to become competitors.

In addition, the Notice asks whether the statutory language could be interpreted to permit separate charges for the two components (transport and termination) of reciprocal compensation.[93] The term "transport and termination" as used in the Act describes the single function of call termination by one LEC of traffic originated by another LEC. Since the 1996 Act imposes the transport and termination obligation on all LECs -- ILEC and competing LECs -- it would be improper to define this function in terms of the historic ILEC network architecture, and to require a rate structure in accordance with that definition.

The concept of mutual and equal compensation requires that rate structures be neutral to the network each carrier chooses to terminate calls. However, in interconnection negotiations, ILECs seek to establish higher rates for traffic terminated through tandem offices than for traffic terminated through end offices,

[92]TW Comm also supports a state's right to define local interconnection for reciprocal compensation beyond the traditional exchange area and EAS boundaries. For example, the New York Public Service Commission has defined local interconnection as LATA-wide.

[93]Notice at ¶231.

arguing that there are additional switching and trunking costs associated with tandem interconnection. Thus, they seek to establish separate rates for the transport through a tandem office and the termination through the end office to the end user. By contrast, the network architectures of many new entrants are quite different. TW Comm's networks, like those of most cable companies and others entering the local exchange market, are characterized by single switches serving entire service areas -- areas which often overlap areas served by numerous ILEC end offices. Because of these differences in network architecture, ILECs' require trunking only to a single competing LEC's switch in order to terminate traffic to all of the competing LEC's customers, while the competing LEC (*e.g.*, TW Comm) must build trunks to many ILEC end offices to terminate traffic to all of the ILEC's customers within the same geographic area, or be subject to significantly higher rates to terminate trunks to one or more ILEC tandem offices.

Transport and termination rate structures based on ILECs' historical choice of network architecture would penalize competing LECs who deploy different architectures, even where the competing LECs' network architecture is more efficient. Based upon TW Comm negotiations with ILECs, the cost to TW Comm for reciprocal compensation may range from $1.25 to $2.50 per line for residential service and from $2.50 to $5.00 per line for business service. These costs are based on assumed balanced traffic and reflect only the additional cost of terminating traffic through ILEC tandem offices. These additional costs, which represent approximately fifteen percent of the available local exchange service revenue, significantly disadvantage new entrants' ability to price compete with ILECs. If the Commission determines that such a rate structure is permissible under the 1996 Act, then the full value of the new entrant's switch that allows call termination to its entire customer base must be recognized and considered as being equivalent to an ILEC tandem switch.[94]

Some ILECs have agreed to flat rate structures for transport and termination but other ILECs have opposed flat rates. TW Comm believes that the 1996 Act allows both flat rate structures and usage-based rate structures. The Commission should require ILECs to offer flat rate structures, but also should permit ILECs and other carriers to agree upon usage-based rate structures. Based upon TW Comm's experiences, the main problem has not been with rate <u>structures</u>, but rather with rate <u>levels</u>. For example, where flat rates are available, those rates typically have been set at levels far above cost of service. For measured use residential service, this means that usage substantially above average levels would need to be generated in order for a new entrant to break even on its

[94]As discussed below, a system of bill-and-keep for mutual compensation for transport and termination would be the most appropriate structure since it would allow all LECs (ILECs and new entrants) to terminate traffic over their networks in the manner deemed to be most efficient for that LEC.

service. For residential service at subsidized flat rates, little, if any, operating margin is available. Therefore, whatever transport and termination rate structure is implemented, the rate levels must be based on LRIC.

2. Congress Established A Pricing Standard For Interconnection And Network Elements That Is Different From The Pricing Standard Established For The Transport And Termination Of Traffic; The Commission's Rules Implementing Pricing Guidelines Should Reflect This Distinction

Section 252(d)(1) of the 1996 Act sets forth a pricing standard by which state commissions are to evaluate the reasonableness of ILEC charges for interconnection and network elements. This standard is to be "based on the cost (determined without reference to a rate-of-return or other rate based proceeding) of providing interconnection or network element[s] ... and may include a reasonable profit."[95]

In contrast, Section 252(d)(2) of the 1996 Act separately sets forth the standards by which state commissions are to evaluate the reasonableness of agreements for reciprocal and mutual compensation between LECs and requesting telecommunications carriers for the transport and termination of traffic pursuant to Section 251(b)(5). Specifically, Congress required that in order to be considered "just and reasonable," the costs associated with the transport and termination of traffic on each carrier's network are to be

[95] Section 252(d)(1)(A).

determined on the "basis of a reasonable approximation of the additional cost of terminating such calls,"[96] *i.e.*, LRIC.

Despite the clear differences between these standards, the Commission raises the possibility that state commissions might use identical pricing rules for interconnection/unbundled network elements and transport/termination.[97] Such a suggestion is clearly at odds with the statutory language. If Congress intended for the same pricing standards to apply, there would have been no need to establish separate language to distinguish charges associated with interconnection and network elements from charges associated with transport and termination. TW Comm therefore urges the Commission to follow the explicit language of Section 252(d)(2) and set pricing standards for transport and termination of traffic at a level equivalent to long run incremental cost of providing such service.

The Notice suggests that transport and termination cannot always be distinguished from network elements. TW Comm believes that the distinction is clear and that any confusion may be attributable to a misunderstanding of what facilities comprise "transport and termination" for purposes of call completion. Whatever facilities are required by the terminating LEC from the interconnection point with the originating LEC are considered

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[96]Section 252(d)(2)(A)(ii).

[97]Notice at ¶¶232-234.

"transport and termination" under the 1996 Act. In most cases, facilities-based service providers will build trunking facilities either to an ILEC end office or to an ILEC tandem office in order to interconnect their networks with those of the ILECs. The Notice suggests that transport and termination cannot always be distinguished from network elements. TW Comm believes that the Commission may misunderstand what facilities comprise "transport and termination" for purposes of call completion. In general, whatever facilities are required by the terminating LEC to complete a call from the interconnection point with the originating carrier are considered "transport and termination" under the 1996 Act. In most instances, facilities-based carriers will build trunking either to an ILEC end office or to a tandem office for purposes of interconnection of networks. The facilities required to terminate calls from this point are what comprise transport and termination, irrespective of a carrier's choice of network design. In other instances, however, carriers may mutually agree to a meet-point arrangement whereby each carrier provides its own facilities to the common meet point. Since this arrangement is mutually agreed upon and each carrier provides its own facilities to the meet point, the transport and termination function would be defined from the common meet point.

Certain new entrants, however, may choose to utilize ILEC dedicated transport facilities between the new entrant's end office and the ILEC tandem or end office. This facility may not only be used for call termination, but also may be used for the provision of other services as well, including, *e.g.*, special access. Under these circumstances, the dedicated transport would be considered a network element because the new entrant had the opportunity either to "make" or "buy" the dedicated facility.[98] The appropriate pricing standard would apply as for other network elements discussed above.

3. The Commission May, And Should, Impose A "Bill and Keep" Compensation Mechanism Pursuant To Its Section 251(d)(1) Authority

One option for meeting the statutory requirement of reciprocal compensation is a "bill-and-keep" (*i.e.*, a zero rate for terminating traffic) approach, whereby each carrier bills its own customers for originating traffic (either on a flat-rate or measured basis), retains all revenues received, and completes traffic originated by connecting carriers without specific charges or compensation. "Bill-and-keep" is not a system of "free" interconnection, but, consistent with the pricing standards outlined in Section 252(d) and discussed above, is a system of mutual and reciprocal compensation which provides each carrier with a tangible benefit. While not receiving an actual cash payment, a

[98]The "buy" may be from a third party vendor other than the ILEC.